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MYTHS ABOUT "LIVING TRUSTS"

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Revocable trusts have become increasingly popular as substitutes for wills in estate planning. Many people believe that by creating a trust, naming themselves as trustees, and transferring their assets to the trust, they will save taxes, simplify the administration of their estates, and save money for their children or other beneficiaries. Unfortunately, these beliefs are not based in fact, and are typical of the myths that surround so-called "living trusts."

Myth # 1: Living trusts save taxes.

This is absolutely wrong. All of the assets in a living trust are subject to both state inheritance taxes and the federal estate tax, just like assets that pass through a probate estate.

A living trust also saves no income taxes during lifetime and may actually *increase* income taxes after death, because some of the income tax rules for trusts are not as favorable as the income tax rules for estates (although an option now exists to elect to treat a revocable trust as part of the probate estate for federal income tax purposes).

A trust that is created *at* death might save taxes in the future in a number of different ways, because a trust can provide income or other benefits to a person without adding those assets to the person's taxable estate, but that kind of trust can be created by will and a revocable trust is not needed.

Myth # 2: A living trust is cheaper to administer than an estate.

This may be true for some persons in some states, but the generalization is wrong more often than it is right.

In Pennsylvania, New Jersey, and many other states, the much-feared "probate of the will" usually takes less than an hour and does not require a lawyer. The real work in the administration of an estate is the collection of the decedent's assets, the payment of debts and death taxes, and the distribution of the remaining assets according to the will. The administration of a living trust is almost exactly the same, because the trust assets must be collected, the debts and death taxes must be paid, and the remaining trust assets must be distributed. The *only* advantage of a living trust is that if the decedent was *not* the trustee, the time and expense of searching for assets and transferring them to the executor might be avoided. That advantage must be weighed against the time and expense of transferring assets to a trustee during lifetime, as well as the inconvenience and loss of control when assets are held in the name of a trustee.

Because the steps necessary to settle a trust are similar to the steps necessary to settle an estate, the legal fees should be about the same, and the executor (or trustee) should be able to negotiate a reasonable fee agreement after comparing the fees of different lawyers. Legal fees for the settlement of an estate will be higher than the fees for the administration of a trust in those few states (such as California and New York) that have complicated probate procedures or a statutory fee schedule for lawyers. In those states, having a living trust may help to reduce legal fees.

Myth # 3: A living trust can be distributed faster than an estate.

This is also wrong. There is no law preventing an executor from distributing all or any part of the estate at any time, as long as the executor is willing to assume the risk of loss if there are additional debts or taxes, or if the distribution is incorrect.

The trustee of a living trust is also liable for debts and taxes, and may delay distributing assets for the same reasons.

As a practical matter, most executors are reluctant to distribute assets until the death taxes have been settled, which can take from nine months to two years, and there is no reason for the trustee of a living trust to distribute assets any more quickly.

Myth # 4: Even if it might do no good, a living trust will do no harm.

Not necessarily.

In their desire to avoid the alleged evils of "probate," many people jump out of the frying pan and into the fire, running directly into the arms of charlatans who are eager to sell "packages" of living trusts for exorbitant fees. And those trust documents may be poorly written, with the result that large fees have been paid for documents that actually result in unnecessary taxes, legal fees, or court costs.

And the probate system is not without its advantages, because it requires notices to beneficiaries and a clear remedy if the estate is not distributed according to the will. In their desire to avoid probate litigation, many people create trusts that give fewer rights to their beneficiaries and so, if the trustee turns out to be dishonest or hostile, the beneficiaries of a living trust may find themselves hampered by the trust document in their attempts to recover their inheritances.

Conclusion: Living trusts are good for some people, but not for everyone.

Living trusts have both advantages and disadvantages, but most people don't need them and aren't helped by them. A living trust is most likely to benefit someone who lives in a state with complicated or expensive estate administration requirements (not Pennsylvania or New Jersey), who has life insurance or retirement benefits which need to be held in trust after death (because of minor children or for tax reasons), who owns real estate in other states (which might require probate proceedings in those other states), or whose investments are already being held and managed by some other person and that other person could serve as trustee at little or no additional cost.

For additional information, see:

- "AARP on Living Trust Scams" and "Living Trusts: Arranging How You Want Your Property Managed Before and After Your Death," both from AARP. AARP also publishes a booklet, "A Consumer's Guide to Living Trusts and Wills" (D14535), a copy of which can be obtained by sending an email request to member@aarp.org. (Be sure to include your name, mailing address, the publication title, and the publication number--D14535.)
- "Beware of Living Trust Scams," a Consumer Advisory from the Attorney General of Pennsylvania.
- "Living Trust Offers: How to Make Sure They're Trust-Worthy" from the Federal Trade Commission.
- "The Truth about Probate & Living Trusts in Pennsylvania" published by the Allegheny County Bar Association.

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